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Supreme Court of the United States

OCTOBER TERM, 1944.

No. 932.

Trust u/w of MARY LILY (FLAGLER) BINGHAM, Messrs. WILLIAM R. KENAN, JR., and LAWRENCE C. HAINES, Trustees,

Petitioners,

against

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

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No. 932.

Trust u/w of MARY LILY (Flagler) BINGHAM, Messrs. William R. Kenan, Jr., and Lawrence C. Haines, Trustees,

Petitioners,

against

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

This is a proceeding to review a judgment of the Circuit Court of Appeals for the Second Circuit which reversed a decision of the Tax Court of the United States. The Tax Court had found that there was no deficiency in the Federal income tax of petitioners for the calendar year 1940. Petition for writ of certiorari was granted on March 12, 1945 (R. 47).

Opinions Below.

The opinion of the Tax Court (R. 26) is reported in 2 T. C. 853. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 41) is reported in 145 F. (2d) 568.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended (28 U. S. C. A., §347(a)).

Statute Involved.

The statute involved is section 121 of the Revenue Act of 1942, c. 619, 56 Stat. 798, which amended section 23(a) of the Internal Revenue Code by adding a new subdivision (2). The relevant portions of section 121 read as follows:

"Sec. 121. Non-Trade or Non-Business Deductions.

"(a) *Deduction for Expenses.*—Section 23(a) (relating to deduction for expenses) is amended to read as follows:

"'(a) *Expenses,*—

'(1) *Trade or Business Expenses.*—

'(A) In General.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

• • • • • •

'(2) *Non-Trade or Non-Business Expenses.*—In the case of an individual, all the ordinary and neces-

sary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income.'

* * * * * *

"(d) *Taxable Years to Which Amendments Applicable.*—The amendments made by this section shall be applicable to taxable years beginning after December 31, 1938."

Section 162 of the Internal Revenue Code (26 U. S. C. A. §162) provides:

"The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual * * *" with exceptions not material here.

The relevant portions of the Reports of Congressional Committees with respect to this section are set forth in the Appendix to this brief at page 31, as are also the pertinent sections of Treasury Regulations 103, at page 36.

Statement of Case.

Petitioners maintain that they were entitled under section 23(a)(2) of the Internal Revenue Code to deduct from gross income for the year 1940 legal fees and disbursements aggregating $25,867.31 as expenses paid "for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income." The Tax Court held on the facts of this case that such deductions were allowable. The Circuit Court of Appeals, without pointing out any clear-cut mistake of law or referring to the decision in *Dobson* v.

Commissioner, 320 U. S. 489 (1943), reversed the Tax Court on the ground that in its opinion these expenses were not sufficiently related to the production or collection of income or the management of income-producing property to come within the statute.

Facts.

All of the facts were stipulated in the Tax Court (R. 10 to 25).

At all times, since prior to January 1, 1940, the taxpayers were the duly qualified and acting trustees of the trust created by the will of Mary Lily (Flagler) Bingham (R. 11).

Mary Lily (Flagler) Bingham died on July 27, 1917 (R. 10), leaving a will executed September 23, 1916 (R. 23). The will (R. 14), after providing for certain devises of real estate and certain specific bequests of jewelry, provides for the conveyance to trustees of all the residue of the property. The trustees were directed to pay to various parties some $536,000 in cash legacies and to deliver to other parties 40,250 shares of stock of various Standard Oil Companies, as soon as compatible with the administration of the estate and the carrying out of the testator's wishes with reference to the hotel and railroad properties mentioned in item NINTH of the will, hereinafter referred to. The will also provided (R. 18) for the payment of $200,000 annually to a niece of the testator until that niece attained the age of 40 years, when she was to be paid $5,000,000 in cash or securities at the discretion of the trustees, if compatible with the interests of the estate. The will also provided (R. 19) that the trustees should pay $75,000 annually to the University of North Carolina

during the continuance of the trust and at the expiration thereof should pay to the University such a sum in cash as would produce an annual income of $75,000.

Item NINTH of the will (R. 19) provided that all the rest of the estate should be held in trust for 21 years from the date of the will for the maintenance and administration and development of the Florida East Coast Railway and the Florida East Coast Hotel properties and the properties held by subsidiary companies. The trustees were given broad powers to administer the trust for this purpose. The will provided for compensation to the trustees of $50,000 a year which should also cover their services as executors (R. 23).

At the end of 21 years from the date of the will the trustees were to divide the property then in their hands into three equal parts and transfer these to the testator's two sisters and brother in equal shares (R. 20).

The trustees of this long-term trust filed an income tax return for the year 1940, showing a tax of $312,629.27, which was duly paid (R. 11).

The Commissioner of Internal Revenue determined a deficiency in income tax for 1940 of $160,815.10 by disallowing the following deductions which had been claimed on the tax return:

Compensation of Trustees	$141,369.86
Office salaries	34,934.30
Office supplies and expenses	2,448.97
Petty cash	1,722.89
Office rent, net	3,419.10
Tax and financial services	498.75
Legal expenses	25,867.31
Miscellaneous	480.75
Total deductions disallowed	$210,741.93

(R. 8).

On the petitioners' petition to the Tax Court, the parties stipulated that, except for the item of $25,867.31 of legal expenses, the expenses originally disallowed were ordinary and necessary expenses paid during the taxable year for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income (R. 11). Such items were therefore deductible under section 23(a)(2) of the Internal Revenue Code, which was added by section 121, Revenue Act of 1942, retroactively applicable to the year 1940.

The legal fees and expenses of $25,867.31 which remained in controversy were as follows:

(1) $16,439.96 was incurred in contesting a deficiency in income tax of the trust of $365,687.12, asserted for the year 1935. This was litigated in the Board of Tax Appeals (*William R. Kenan, Jr., et al.*, 40 B. T. A. 824 (1939)) and the Circuit Court of Appeals for the Second Circuit (*Kenan* v. *Commissioner*, 114 F. (2d) 217 (1940)). In this proceeding, the Courts sustained the Commissioner in holding that the trustees realized a gain from the sale or exchange of capital assets by exercising their power to pay partly in securities at market value the bequest of $5,000,000 payable to the testator's niece when she reached age 40 or as soon thereafter as compatible with the interests of the estate. The securities so delivered had appreciated in value since acquisition by the trustees and it was held that such delivery in satisfaction of this bequest, although within the discretionary powers of the trustees, was nevertheless a sale or exchange of the securities, giving rise to capital gain (R. 29).

(2) $780.85 was for services and disbursements in connection with the payment at the termination of the trust

of the above mentioned legacy to the University of North Carolina (R. 30).

(3) The remaining $8,646.50 of the total of $25,867.31 in legal fees and charges paid by the petitioners in 1940 was for services rendered in respect of the tax and other problems resulting from the expiration of the trust and the delivery of its assets to the legatees (R. 30).

The Commissioner conceded in his brief in the Tax Court that the trust property was held for the production of income, as those words are used in section 23(a)(2) of the Internal Revenue Code (R. 33) and there was no claim that the expenses were not ordinary and necessary (R. 33).

The Decisions Below.

The Tax Court, on the facts of this case, held in an opinion reviewed by the full Court that the legal expenses were deductible under section 23(a)(2) (R. 26). Two Judges dissented (R. 36). The Tax Court first refused to allow the expenses as expenses of carrying on a trade or business (R. 31). No appeal was taken from this part of the decision. The Tax Court then held that the $16,439.96 expense of the income tax litigation was deductible because it found that the effort of these trustees to relieve the estate from the payment of this tax was a factor in the management, conservation, and maintenance of the property of that estate, concededly held for the production of income (R. 33). Two Judges, who concurred in the result, did not adopt this ground for the decision (R. 35). The Tax Court then found that all the expenses (including the expense of the tax litigation) were incurred by the trustees in the performance of one of the principal functions of the management of such property while they were in complete

control of it, and that such expenses were deductible as expenses for the management of property held for the production of income (R. 33, 34).

The Circuit Court of Appeals reversed this decision (R. 45). The Court mentioned, but did not pass on, the Commissioner's contention that the expenses were in the nature of capital expenditures (R. 43). It based its decision on the ground that the expense of contesting the taxes "had no relation" to the management, conservation, or maintenance of property held for the production of income because the contest was not to produce income and did not affect the yield of investment capital or its appreciation (R. 43); it said that the expense of $780.85 for services in connection with the payment to the University of North Carolina "had no relation" to the production of income, or to the conservation of the property held for that purpose because it had to do with distribution and not with management (R. 44); it said that the remaining expenses of $8,646.50 were likewise paid in connection with distribution of trust assets and not with the production of income or the management of the property, were paid for services performed after the trust had ended, and that the advice "involved personal services rather than management of the trust estate" (R. 44).

The essential point of difference between the Tax Court and the Circuit Court of Appeals was that the former found that these expenses were directly connected with or related to the management of the property of this trust, whereas the latter found that such expenses bore "no relation" to such management.

Specification of Errors.

1. Under the principles established in *Dobson* v. *Commissioner*, 320 U. S. 489 (1943), the Circuit Court of Appeals

erred in reversing the decision of the Tax Court that certain legal expenses of this trust were expenses for management of income-producing property deductible under section 23(a)(2), on the ground that such expenses bore no relation to such management. The relation of such expenses to the management of the income-producing property was a question of fact as to which the decision of the Tax Court should have been regarded as final.

2. Whatever view is taken as to the finality of the Tax Court's determination of fact, the Tax Court made no "clear-cut mistake of law" in holding that legal expenses of this trust incurred in winding up the trust and distributing its assets and in contesting the income tax effect of a transfer of income-producing property to a beneficiary were expenses for the management of the trust property.

Summary of Argument.

The Tax Court in a carefully considered opinion, reviewed by the entire Court, held that the expenses here in controversy were expenses "for the management, conservation, or maintenance of property held for the production of income" deductible under section 23(a)(2). The Circuit Court of Appeals, without indicating any clear-cut mistake of law or referring to *Dobson* v. *Commissioner*, 320 U. S. 489 (1943), reversed on the ground that such expenses had no relation to the production or collection of income or the management, conservation, or maintenance of property held for the production of income. The relationship of the expenses to the management of property held for the production of income was a question of fact. Under the principles as to appellate procedure established by this Court the factual determination of the Tax Court if

supported by substantial evidence, was not subject to review (*Dobson* v. *Commissioner*, 320 U. S. 489 (1943); *Commissioner* v. *Scottish American Investment Co., Ltd.*, 323 U. S. 119 (1944)).

The decision of the Tax Court involved no clear-cut mistake of law, was supported by substantial evidence, was in any case not without rational basis and was not contrary to any statute, any regulation having the force of law or any established legal principle.

The petitioners were the trustees of a large long-term trust holding property for the production of income. The expenses were ordinary and necessary. The nature of the expenses and their relationship to the management of the trust property were shown in detail. Everything the trustees did was pursuant to their duties in handling the property while subject to their complete control. The settling up by the trustees of this trust holding property for the production of income was an important and essential part of the management of such property.

The decision of the Tax Court does not contravene the provisions of section 23(a)(2) and the deduction allowed falls within its clear provisions. The statute allows not only the deduction of expenses "for the production or collection of income" but also of expenses "for the management, conservation, or maintenance of property held for the production of income." Congress intended to allow the deduction of all ordinary and necessary expenses incurred in the pursuit of income or in connection with property held for the production of income. The term "management" plainly includes the expenses of settling up a long-term trust holding property for the production of income, including the expense of litigating a claim that the delivery of property to a beneficiary pursuant to the terms of the will gave rise to taxable income.

The statute cannot properly be construed so as to narrow the deduction for expenses of management of property held for the production of income to the portion of such expenses incurred "for the production or collection of income." Where a long-term trust for the management of property held for the production of income is employed, a common practice, the management expenses involved in the necessary settling up of the trust are included in the allowable deductions.

The decision of the Tax Court does not contravene any regulation having the force of law. The regulations with respect to the deductibility of administration expenses of administrators and executors in handling an estate in process of administration are not applicable to the management expenses of trustees of a long-term trust. Administration expenses, which are primarily deductible in determining the gross estate subject to estate tax rather than net income subject to income tax, differ fundamentally from the expenses of managing a long-term trust of property held for the production of income. The trustees' management expenses here involved, including the expenses of settling up the trust, were not capital expenditures since they were not paid for the acquisition of any property and were not additions to cost of any property.

The decision of the Tax Court does not contravene any established legal principle. There is no established principle that expenses of income tax controversies of trustees not engaged in trade or business are not deductible under any facts or circumstances unless directly connected with the production or collection of income. In any particular case, such as this, where such expenses are ordinary and necessary expenses of management of property held for the production of income, they are deductible

under the clear provisions of section 23(a)(2) and of the Commissioner's regulation as to trustees' deductions. The question in each case is one of fact for final determination by the Tax Court.

ARGUMENT.

I.

The Circuit Court of Appeals erred in reversing the decision of the Tax Court that certain legal expenses of this trust were expenses for the management of income-producing property deductible under section 23(a) (2) on the ground that such expenses bore no relation to such management. The relation of such expenses to the management of the income-producing property was a question of fact as to which the decision of the Tax Court should have been regarded as final.

In this case the Tax Court, in a carefully considered opinion reviewed by the entire Court, found that the expenses in controversy were incurred by the trustees as an important part of their duties and functions in managing the trust property while they were in complete control of it, and that such expenses were "for the management * * * of property held for the production of income" and hence deductible under section 23(a) (2) of the Internal Revenue Code as added by section 121(a) of the Revenue Act of 1942 (R. 35).

The Circuit Court of Appeals reversed because it differed with the Tax Court as to the relationship of the expenditures to the management of the property held for the production of income. It took the view that the expenses

"had nothing to do with the production of taxable gain or ordinary income" (R. 43) and "had no relation" to the production of income or the management of property held for the production of income (R. 43, 44).

The merits and detailed facts of the case are discussed in point II below. Irrespective of these, it is submitted that the reversal of the Tax Court's decision by the Circuit Court of Appeals was erroneous under the principles as to appellate power set forth in *Dobson* v. *Commissioner*, 320 U. S. 489 (1943) and *Commissioner* v. *Scottish American Investment Co., Ltd.*, 323 U. S. 119 (1944). The power of appellate courts upon review of Tax Court decisions is a "power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require". (Section 1141(c)(1), Internal Revenue Code, 44 Stat. 110.)

The relationship of these expenses to the management of the property held by these trustees for the production of income is purely a question of fact, as to which the Tax Court's decision if supported by substantial evidence, is final.

Every case in which the deduction of expenses is claimed involves a question of fact as to whether such expenses are incurred "in carrying on any trade or business" if the claim is made under section 23(a) (1), or are incurred "for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income" if the claim is made under section 23(a)(2). The factual inference or conclusion of the Tax Court on the facts of particular cases as to whether or not the expenses are incurred for the purposes designated in the statute is obviously of little value as a precedent in other

cases and, under controlling decisions of this Court, is not subject to review.

In *Dobson* v. *Commissioner*, 320 U. S. 489 (1943), the Court said (p. 502):

> "when the court cannot separate the elements of a decision so as to identify a clear-cut mistake of law, the decision of the Tax Court must stand. • • • Where no statute or regulation controls, the Tax Court's selection of the course to follow is no more reviewable than any other question of fact."

In *Commissioner* v. *Heininger*, 320 U. S. 467, 475 (1943), the Court said, in a controversy as to the deduction of business expenses:

> "Whether an expenditure is directly related to a business and whether it is ordinary and necessary are doubtless pure questions of fact in most instances. Except where a question of law is unmistakably involved a decision of the Board of Tax Appeals on these issues, having taken into account the presumption supporting the Commissioner's ruling, should not be reversed by the federal appellate courts. Careful adherence to this principle will result in a more orderly and more uniform system of tax deductions in a field necessarily beset by innumerable complexities."

In that case the Court reversed the Board of Tax Appeals solely because it had proceeded on a mistaken conviction that denial of the deduction claimed was required as a matter of law.

In *McDonald* v. *Commissioner*, 323 U. S. 57 (1944), involving the deductibility of campaign expenses of a state judge seeking election, the Court affirmed a decision of the Tax Court denying the deduction. After discussing the

question of statutory construction involved, the Court said at pages 64-65:

> "Even if these conclusions, in the setting of federal income tax legislation, derived less easily than they do from the statutory provisions under scrutiny, we should not be inclined to displace the views of the Tax Court with our own. Of course the Tax Court cannot define the limits of its own authority. And in cases like *Commissioner* v. *Heininger*, 320 U. S. 467, where the Tax Court mistakenly felt itself bound by superior judicial authority, we must give corrective relief. But, as a system, tax legislation is not to be treated as though it were loose talk or presented isolated abstract questions of law casting upon the federal courts the task of independent construction. Tax language normally has an enclosed meaning or has legitimately acquired such by the authority of those specially skilled in its application. To speak of tax determinations made in the system of review specially designed for federal tax cases as technical is not to imply opprobrium.
>
> Having regard to the controversies which peculiarly call for this Court's adjudication and to the demands for their adequate disposition, as well as to the exigencies of litigation generally, relatively few appeals from Tax Court decisions can in any event come here. That court of necessity must be the main agency for nation-wide supervision of tax administration. Whatever the statutory or practical limitations upon the exercise of its authority, Congress has plainly designed that tribunal to serve, as it were, as the exchequer court of the country. Due regard for these considerations is the underlying rationale of *Dobson* v. *Commissioner*, 320 U. S. 489. We are therefore relieved from discussing the numerous cases in which the Tax Court or its predecessor, the Board of Tax Appeals, allowed or disallowed deductions and their bearing on the situation before

> us. To do so involves detailed analysis of the special circumstances of various 'businesses' and expenses incident to their 'carrying on'. We shall not enter this quagmire of particularities."

In the dissenting opinion in the same case, at page 66, it is said:

> "Were the expenses incurred in an effort to produce income? Were these expenses, or part of them, 'ordinary and necessary' in connection with that effort? These are in most instances pure questions of fact and in cases such as this are to be determined by the Tax Court."

In *Commissioner* v. *Wemyss*, No. 629, October Term 1944, decided March 5, 1945, the Court, after stating in detail how the Tax Court dealt with the problem of the liability for gift tax, where an ante-nuptial gift was made because upon remarriage the income from a pre-existing trust would no longer be received by the prospective wife but would pass to her son, said:

> "The Tax Court in effect found the transfer of the stock to Mrs. More was not made at arm's length in the ordinary course of business. It noted that the inducement was marriage, took account of the discrepancy between what she got and what she gave up, and also of the benefit that her marriage settlement brought to her son. These were considerations the Tax Court could justifiably heed, and heeding decide as it did. It's conclusion on the issue before it was no less to be respected than were the issues which we deemed it was entitled to decide as it did in *Dobson* v. *Commissioner*, 320 U. S. 489, *Commissioner* v. *Heininger*, 320 U. S. 467, *Commissioner* v. *Scottish American Co.*, 323 U. S. 119."

See also *Commissioner* v. *Court Holding Company*, No. 581, October Term 1944, decided March 12, 1945.

Since the factual decision of the Tax Court—that the expenses in this case were sufficiently related to the management of property held for the production of income to be deductible—would be of little value as a precedent in other cases involving different facts, the case is of the type referred to in *Commissioner* v. *Scottish American Investment Co., Ltd.*, 323 U. S. 119, 125 (1944).

> "Moreover, this case exemplifies one type of factual dispute where judicial abstinence should be pronounced. The decision as to the facts in this case, like analogous ones that preceded it, is of little value as precedent. The factual pattern is too decisive and too varied from case to case to warrant a great expenditure of appellate court energy on unraveling conflicting factual inferences."

Under these principles, the decision of the Circuit Court of Appeals should be reversed because, without pointing out any clear-cut mistake of law or referring to the *Dobson* case, it reversed a decision of the Tax Court as to a purely factual question. The decision of the Circuit Court of Appeals is clearly contrary to the principles as to judicial review of Tax Court decisions established by this Court.

II.

Whatever view is taken as to the finality of the Tax Court's determination of fact, the Tax Court made no "clear-cut mistake of law" in holding that expenses of this trust incurred in winding up the trust and distributing its assets and in contesting the income tax effect of a transfer of income-producing property to a beneficiary were expenses for the management of the trust property.

Petitioners, of course, maintain, as they did before the Tax Court, that the expenses in question were clearly deductible under the statute.

We submit that in any case the decision of the Tax Court involved no "clear-cut mistake of law," was supported by substantial evidence, was not without rational basis and was not contrary to any statute, any regulation having the force of law or any established legal principle, and should therefore be affirmed.

The petitioners in this case were not individuals, but the trustees of a long-term testamentary trust. It was conceded by the Commissioner in the Tax Court that the trust property was "held for the production of income, as those words are used in section 23(a) (2)" (R. 33). The trust was obviously a large one, as it reported and paid income taxes of $312,629.27 for 1940 (R. 11), and the trustees received compensation in that year of $141,369.86, which the Commissioner stipulated was an expense for the management of property held for the production of income (R. 11, 12). The Tax Court states: "There is no dispute over whether the claimed deductions were ordinary and necessary expenses" (R. 33). The exact nature of the expenses

in controversy and their relationship to the handling of the trust property are shown in detail. It was not denied that everything the trustees did was pursuant to their powers and duties as trustees and that the expenditures were incurred while the property was under their complete control (R. 34). The Commissioner stipulated that all of the expenses originally disallowed, except the legal expenses, were within section 23(a)(2), making no attempt to allocate any part of the compensation of the trustees and their employees, the rent or other expenses, to the work done in settling up the trust pursuant to the provisions of the will.

On the basis of these facts the Tax Court approved the deduction as expenses of "management * * * of property held for the production of income" of the items here in question, as follows:

Deduction of the $16,439.96 of legal fees and charge paid in contesting a 1935 income tax deficiency of $365,687.12 was first approved on the following ground:

> "The effort of petitioners in seeking, through this litigation, to give such *relief to the estate*"—relief from payment of the deficiency in income tax—"was, in our opinion, obviously a factor in the conservation, management and maintenance of the property of the estate, concededly held for the production of income, since in resisting the imposition of the tax the trustees were performing the required duty of protecting and defending the trust property in their hands against any claim or lien for the tax" (R. 33). (Italics supplied.)

This same item of $16,439.96 and the additional expenses of $9,427.35 were approved as deductions by the Tax Court on the ground that they were all "expenses paid for the 'management' of the property" (R. 33).

The additional expenses involved problems arising out of the payment of the bequest to the University of North Carolina, the expiration of the trust and the distribution of its assets to the legatees (R. 30). The Tax Court said:

> "such payment and distribution were made by the trustees as directed by the will and as a part of their duties in managing the trust property" (R. 34).

The Tax Court further said that the expenses of "settling up" the trust estate were deductible

> "since one, if not the most, vital duty imposed on those trustees was to make proper distribution of such property, and in making it they were performing one of the principal functions of the management of such property, since until that property reached the hands of the legatees and distributees the trustees were in complete control of it, and thus its management" (R. 34).

The concurring Judges agreed that all the expenses in controversy were deductible on the ground that "the management of the property of the estate embraced the proper disposition of it pursuant to the will of the decedent" (R. 35).

We submit that there was substantial evidence to support the Tax Court's decision that, under the statute, such expenses were for the management of property held for the production of income and that under the facts of this case such decision was not unreasonable or without rational basis.

The decision of the Tax Court did not contravene the provisions of the statute.

Section 23(a)(2) has two branches. The section (1) allows the deduction of ordinary and necessary expenses "for the production or collection of income" and (2) the deduction of ordinary and necessary expenses for the "management, conservation, or maintenance of property held for the production of income." Both clauses must be given effect and the second clause cannot be narrowed to include only expenses "for the production or collection of income."

The Committee Reports show that what Congress intended was to allow the deduction of ordinary and necessary expenses incurred in connection with investment income and property, thus curing the inequity of the prior statute made manifest by the decision in *Higgins* v. *Commissioner*, 312 U. S. 212 (1941).

The House Report, set forth in full in the Appendix, page 31, says in part:

> "Thus whether or not the expense is in connection with the taxpayer's trade or business, if it is expended in the pursuit of income or in connection with property held for the production of income, it is allowable." (Appendix, p. 31)

The Report further says:

> "Expenses incurred in managing or conserving property held for investment may be deductible under this provision even though there is no likelihood that the property will be sold at a profit or will otherwise be productive of income." (Appendix, p. 32)

The Senate Report (Appendix, p. 34) is to the same effect.

The purpose of Congress clearly was to provide that as to investment income as well as to business income, the tax

would fall on "net income" and not on "gross income." The taxpayer was not required to prove that each expense had the direct purpose or result of producing income. The expense was deductible if incurred in connection with income-producing property and the broad words "management, conservation, or maintenance" were used. Such an expense was deductible even though there was no likelihood that gain or other income would actually be produced.

Although a statute allowing a deduction must be strictly construed (*New Colonial Ice Co., Inc.* v. *Helvering*, 292 U. S. 435 (1934); *Equitable Society* v. *Commissioner*, 321 U. S. 560, 564 (1944)), such a statute is not an exemption statute as the section here involved is characterized below (R. 44) and this Court has indicated that the rule means no more than that a statute allowing deductions covers only those items which "can conveniently come within" its "clear provision." (*McDonald* v. *Commissioner*, 323 U. S. 57, 60 (1944)).

The word "management" plainly includes the activities of the trustees of a long-term trust of property held for the production of income in settling up the trust and distributing its assets and in litigating an income tax controversy arising out of a distribution of income producing property held to give rise to taxable gain. "Management" is a word of comprehensive meaning and includes administration, care, carrying on, control, direction, etc. (38 C. J. 524). The word "manage" means "To control and direct; to handle successfully or cope with; to conduct; guide; administer" (Webster's New International Dictionary, Second Edition). "Management," as used in section 23(a)(2), is not confined in its meaning to "holding" or "operating." It necessarily includes a transfer of property by sale or exchange giving rise to capital gain,

such as the distribution to the testator's niece, which was held to be an exchange giving rise to gain. Similarly, the transfer of property upon the termination of the trust and the settlement of all the problems rising in connection therewith were an essential and important part of the management of the trust property.

The Circuit Court of Appeals, in so far as it purported to construe the statute, apparently took the view that expenses of "management" were deductible only if that particular phase of the handling of the property was designed to produce gain or income. Thus, the Court said with respect to the expense of the income tax litigation (R. 43):

> "It was not made as a recompense for management or maintenance of the trust property since that property was not held for the production of income but was in the hands of the trustees ready for distribution. Taxes laid upon it had nothing to do with the production of taxable gain or ordinary income. The expense of contesting the taxes had no relation to the 'management, conservation or maintenance of property held for the production of income.' The contest was not in order to produce income and the expenditure, accordingly, has no bearing upon such a purpose. To be deductible as expenses for management they must relate to the production of income or to the maintenance of property held for that purpose. They were not deductible when incurred merely to prevent the incidence of taxes which neither affected the yield of invested capital nor its appreciation."

This view that management expenses are deductible only if they are expenses incurred "for the production of income" is not supported by the language of the statute and

gives no effect to the second clause allowing the deduction of expenses "for the management, conservation, or maintenance of property held for the production of income." The latter clause cannot properly be so limited in its application as to mean no more than does the first clause.

The establishment of a long-term trust is a common method employed for the management of income-producing property. In every such case expense is involved in connection with the winding up of the trust, the distribution of the trust properties and the accounting to the beneficiaries at the termination of the trust. The trustees and their employees, accountants and attorneys must devote time and attention to this most important function and activity. This is an essential part of the management of the trust, and where the trust consists of property held for the production of income these expenses are properly deductible from income. Taxpayers are not required by the statute to analyze management expenses to determine which part of such expenses were incurred "for the production of income." All ordinary and necessary expenses of management of income-producing property are deductible.

The decision of the Tax Court does not contravene any regulation having the effect of law.

The Commissioner, when section 23(a)(2) was enacted, issued a long and comprehensive regulation (section 19.23(a)-15, Regulations 103) which is set forth in the Appendix, p. 36. There was at that time in effect a long-standing regulation with reference to "capital expenditures" (section 19.24-2) which is also set forth in the Appendix, p. 43. In opposition to the granting of the petition for certiorari the respondent claimed that the Tax Court's decision was contrary to these regulations. The Circuit Court of Appeals in its opinion below did not adopt this ground for decision.

The difficulty with this contention is that the respondent is relying on regulations with respect to the expenses of *administrators and executors* in administering an estate, which are primarily deductible in computing the gross estate, subject to estate tax and generally not deductible for income tax purposes. The expenses here in question are not expenses of the administration of an estate, which are deductible in computing an estate tax. They are expenses of trustees managing property held for the production of income and are deductible only from income. Hence the regulations referred to are inapplicable. (*Estate of Frederic E. Baldwin*, 44 B. T. A. 900 (1941); *Estate of John B. Sharpe* v. *Commissioner*, C. C. A. 3rd, March 6, 1945, not yet officially reported.)

The respondent relies on the following portions of the regulations. Section 19.23(a)-15, the new regulation promulgated under section 23(a)(2), provides in part (Appendix, p. 40):

> "Expenditures incurred by an administrator or executor in securing the processes and orders of the court having jurisdiction over the probate of the estate, or in collecting the assets of the estate (other than income which, if and when realized, must be reported by the estate for income tax purposes), or in adjusting claims against the decedent, or in distributing the remaining assets to the beneficiaries, or in conserving the assets for ultimate distribution to the parties entitled thereto, are not deductible under this section."

Section 19.24-2 of Regulations 103, Appendix, p. 43, which was in effect when the new regulation was promulgated merely provided in part:

> "Expenses of the administration of an estate, such as court costs, attorneys' fees and executors' com-

missions, are chargeable against the corpus of the estate and are not allowable deductions."

Both the new and the old regulation relied on by the respondent have to do only with expenses of administration incurred by an *administrator or executor*, and have no application to the present controversy.

The new regulation under section 23(a)(2) contains an entirely separate provision as to the expenses of *trustees*, which reads as follows (Appendix, p. 41):

> "Reasonable amounts paid or incurred by a trustee on account of trustees' fees and other expenses which are ordinary and necessary in connection with the production or collection of trust income or with the management, conservation, or maintenance of trust property held for the production of income are deductible, notwithstanding that the trust is not engaged in a trade or business."

This regulation as to *trustees* follows substantially the language of the statute allowing broadly to trustees the deduction of expenses "in connection with the production or collection of trust income or with the management, conservation, or maintenance of trust property." This is the controlling regulation in the present case.

The expenditures here in controversy are not capital expenditures such as were involved in *Bowers* v. *Lumpkin*, 140 F. (2d) 927 (C. C. A. 4th, 1944), cert. den. 322 U. S. 755, and *Helvering* v. *Stormfeltz*, 142 F. (2) 982 (C. C. A. 8th, 1944). Capital expenditures are "Any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate." (Section 24(a)(2), Internal Revenue Code.) Capital expenditures represent the cost of acquiring property or title and are added to the cost. No asset of this trust

was acquired nor was its cost to anyone increased by reason of the expenditures here in controversy. They were expenses of handling or managing the property pursuant to the plan set up in the testator's will.

The decision of the Tax Court was not contrary to any established legal principle.

Giving no effect to the express provisions of the statute, the respondent may contend that under no factual circumstances can expenses of contesting income tax matters be regarded as incurred for the management, conservation, or maintenance of property held for the production of income, and that such expenses are never deductible by taxpayers not engaged in trade or business except to the extent that the recovery of taxable interest is involved. This is the position which the Commissioner seems to have taken in one portion of section 19.23(a)-15 of Regulations 103 reading as follows:

> "Expenditures incurred for the purpose of preparing tax returns (except to the extent such returns relate to taxes on property held for the production of income), for the purpose of recovering taxes (other than recoveries required to be included in income), or for the purpose of resisting a proposed additional assessment of taxes (other than taxes on property held for the production of income) are not deductible expenses under this section, except that part thereof which the taxpayer clearly shows to be properly allocable to the recovery of interest required to be included in income" (Appendix, p. 42).

If by this portion of the regulation the Commissioner means to rule that under no circumstances can trustees not engaged in business deduct expenses in connection with income tax returns and controversies except to the extent

that such expenses are incurred "for the production of income," the regulation is not in conformity with the statute and is inconsistent with the portion of the regulation quoted at page 26 above, which, as provided in the statute, permits trustees to deduct expenses incurred "for the management, conservation, or maintenance of trust property held for the production of income."

The Circuit Court of Appeals in its opinion below erroneously intimates that trustees can never deduct expenses of litigation over income taxes as expenses of management of the trust properties because they have to do with past transactions and do not affect the yield of investment capital or its appreciation (R. 44).

The cases cited by the Circuit Court of Appeals, in all of which the Tax Court or its predecessor was affirmed, establish no such rule of law. In *Stoddard* v. *Commissioner*, 141 F. (2d) 76 (C. C. A. 2nd, 1944), the decision simply was that an individual taxpayer could not deduct expenses of contesting prior years' income taxes where there was no proof of the nature of the controversy. (See 47 B. T. A. 584, 588). In *Higgins* v. *Commissioner*, 143 F. (2d) 654 (C. C. A. 1st, 1944), the Court refused to hold that the statute in all cases allowed as expenses of management the deduction of expenses in connection with individual income tax controversies, the Court's view being that the deductibility of such an item was a question of fact in each case. In *Hord* v. *Commissioner*, 143 F. (2d) 73 (C. C. A. 6th, 1944), the expenses disallowed were with respect to a controversy over an undescribed income tax refund for 1928 and the determination of an undescribed deficiency for 1929. In none of these cases did the proof submitted establish any connection between the expenses claimed and the management of property held for the production of income.

The Tax Court was, of course, familiar with these decisions. It has nevertheless in this and in other cases, on the submission of proper proof, allowed the deduction of expenses of income tax controversies, particularly where, as in this case, the controverted transaction was one which itself gave rise to taxable income. *Charles H. Manning*, 3 T. C. 853, 874 (No. 108) (1944). The Tax Court there said that if the "original transaction was proximately related to the production or collection of income, any litigation arising out of that transaction involving its tax consequences would also proximately relate to the production or collection of income." This view is confirmed in *Estate of Frederick Cecil Barthelomew*, 4 T. C. No. 44 (1944), and is supported by the reasoning in *Kornhauser* v. *United States*, 276 U. S. 145 (1928).

The question is not one of general policy, as such expenses are, of course, fully deductible by corporations and by individuals, partnerships or trusts carrying on or doing business. There is no reason of policy for denying such deductions to individuals or trusts having investment income if otherwise they fall within the terms of the statute.

The Tax Court has held that the legal expenses of these trustees, which are here in controversy, were, under the facts of this case, expenses for the management of property held for the production of income. Such expenses of management are deductible under the clear provisions of the statute and of the Commissioner's regulation as to deductible expenses of trustees.

Conclusion.

For the foregoing reasons it is respectfully submitted that the judgment of the Circuit Court of Appeals for the Second Circuit should be reversed and the decision of the Tax Court affirmed.

Respectfully submitted,

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Appendix.

H. Rep. No. 2333, 77th Cong., 2nd Sess., pp. 46, 74-76:

6. Nontrade or Nonbusiness Deductions

The existing law allows taxpayers to deduct expenses incurred in connection with a trade or business. Due partly to the inadequacy of the statute and partly to court decisions, nontrade or nonbusiness expenses are not deductible, although nontrade or nonbusiness income is fully subject to the tax. The bill corrects this inequity by allowing all of the ordinary and necessary expenses paid or incurred for the production or collection of income or for the management, conservation or maintenance of property held for the production of income. Thus, whether or not the expense is in connection with the taxpayer's trade or business, if it is expended in the pursuit of income or in connection with property held for the production of income, it is allowable.

Section 118. Nontrade or Nonbusiness Deductions.

This amendment allows a deduction for the ordinary and necessary expenses of an individual paid or incurred during the taxable year for the production and collection of income, or for the management, conservation, or maintenance of property held by the taxpayer for the production of income, whether or not such expenses are paid or incurred in carrying on a trade or business, and also allows a deduction for the exhaustion and wear and tear (including a reasonable amount for obsolescence) on property held for the production of income, whether or not such property is used by the taxpayer in a trade or business.

For an expense to be deductible under this section, it must have been incurred either (1) for the production or collection of income, or (2) for the management,

conservation, or maintenance of property held for the production of income. Ordinary and necessary expenses so paid or incurred are deductible under section 23 (a)(2) even though they are not paid or incurred for the production or collection of income of the taxable year or for the management, conservation, or maintenance of property held for the production of such income. The term "income" for this purpose comprehends not merely income of the taxable year but also income which the taxpayer has realized in a prior taxable year or may realize in subsequent taxable years, and is not confined to recurring income but applies as well to gain from the disposition of property. Expenses incurred in managing or conserving property held for investment may be deductible under this provision even though there is no likelihood that the property will be sold at a profit or will otherwise be productive of income. The expenses, however, of carrying on a transaction which does not constitute a trade or business of the taxpayer and is not carried on for the production of income or for the management, conservation, or maintenance of property, but which is carried on primarily as a sport, hobby, or recreation are not allowable as nontrade or nonbusiness expenses.

Expenses to be deductible under Section 23 (a)(2), must be ordinary and necessary, which rule presupposes that they must be reasonable in amount and must bear a reasonable and proximate relation to the production or collection of income, or to the management, conservation, or maintenance of property held for that purpose.

A deduction under this section is subject, except for the requirement of being incurred in connection with a trade or business, to all the restrictions and limitations that apply in the case of the deduction under section 23 (a) (1) (A) of an expense paid or incurred in carrying on any trade or business. Section 24 (a) (5), as amended by this section, while continuing to disallow any amount allowable as a deduction,

whether under section 23 (a) (2) or otherwise, which is allocable to one or more cases of tax-exempt income, other than interest, has the effect in addition of disallowing a deduction under section 23 (a) (2) for amounts allowable under that section which are allocable to tax-exempt interest.

Expenses incurred by an administrator or executor in the administration of the estate of a decedent, such, for example, as expenses in securing the processes and orders of the court having jurisdiction over the probate of an estate, or in adjusting claims against the estate, or in distributing the remaining assets to the beneficiaries, are not deductible under this section. Ordinary and necessary expenses, however, which are paid or incurred during the taxable year by an administrator or an executor for the production or collection of income which must be reported by the estate for income tax purposes, may be claimed as deductions under this section notwithstanding that deductions therefor are allowable under section 812 (b) in computing the gross estate subject to the estate tax. Accordingly, subsection (c) of this section amends section 162 to provide that no deduction shall be allowed under section 23 (a) (2) in computing the net income of the estate for amounts for which there may have been or has already been allowed a deduction under section 812 (b) in computing the net estate of the decedent. The present amendment would not allow as a deduction under section 23 (a) (2) for income tax purposes any amount which is allowable under section 812 (b) as a deduction in computing the net estate of a decedent for estate tax purposes, unless the Commissioner receives a statement, filed within the time and in the manner and form prescribed by him, to the effect that the amount in question has not been claimed or allowed as a deduction under section 812 (b) and that the right to have such items allowed at any time as a deduction under section 812 (b) is waived.

Subsection (d) of this section amends section 23 (1) of the Internal Revenue Code so as to allow, in addition to the deduction allowable under the existing law, a deduction for the exhaustion, wear and tear of property held by the taxpayer for the production of income, whether or not the property in question is used in the trade or business of the taxpayer, including a reasonable allowance for obsolescence. Except for this, the new allowance is subject to the same limitations and restrictions which have been applicable under this section prior to the present amendment.

The amendments made to the Internal Revenue Code by this section are applicable to all taxable years beginning after December 31, 1938. These amendments shall also be effective as if they were a part of the Revenue Act of 1938 or any prior revenue act on the date of its enactment.

S. Rep. No. 1631, 77th Cong., 2nd Sess., pp. 87-88:

SECTION 121. NON-TRADE OR NON-BUSINESS DEDUCTIONS.

This section is the same as section 118 of the House bill, except that subsection (c) of that section has been omitted therefrom and now appears as section 163 and a clerical amendment has been made in subsection (b). The amendment made by this section allows a deduction for the ordinary and necessary expenses of an individual paid or incurred during the taxable year for the production and collection of income, or for the management, conservation, or maintenance of property held by the taxpayer for the production of income, whether or not such expenses are paid or incurred in carrying on a trade or business, and also allows a deduction for the exhaustion and wear and tear (including a reasonable amount for obsolescence) on property held for the production of income, whether or not such property is used by the taxpayer in a trade or business.

For an expense to be deductible under this section, it must have been incurred either (1) for the production or collection of income, or (2) for the management, conservation, or maintenance of property held for the production of income. Ordinary and necessary expenses so paid or incurred are deductible under section 23 (a) (2) even though they are not paid or incurred for the production or collection of income of the taxable year or for the management, conservation, or maintenance of property held for the production of such income. The term "income" for this purpose comprehends not merely income of the taxable year but also income which the taxpayer has realized in a prior taxable year or may realize in subsequent taxable years, and is not confined to recurring income but applies as well to gain from the disposition of property. Expenses incurred in managing or conserving property held for investment may be deductible under this provision even though there is no likelihood that the property will be sold at a profit or will otherwise be productive of income, and even though the property is held merely to minimize a loss with respect thereto. The expenses, however, of carrying on a transaction which does not constitute a trade or business of the taxpayer and is not carried on for the production of income or for the management, conservation, or maintenance of property, but which is carried on primarily as a sport, hobby, or recreation are not allowable as non-trade or non-business expenses.

Expenses, to be deductible under section 23 (a) (2), must be ordinary and necessary, which rule presupposes that they must be reasonable in amount and must bear a reasonable and proximate relation to the production or collection of income, or to the management, conservation, or maintenance of property held for that purpose.

A deduction under this section is subject, except for the requirement of being incurred in connection with a trade or business, to all the restrictions and

limitations that apply in the case of the deduction under section 23 (a) (1) (A) of an expense paid or incurred in carrying on any trade or business. Section 24 (a) (5), as amended by this section, while continuing to disallow any amount allowable as a deduction, whether under section 23 (a) (2) or otherwise, which is allocable to one or more classes of tax-exempt income, other than interest, has the effect in addition of disallowing a deduction under section 23 (a) (2) for amounts allowable under that section which are allocable to tax-exempt interest.

Subsection (c) of this section amends section 23 (l) of the Code so as to allow, in addition to the deduction allowable under the existing law, a deduction for the exhaustion, wear, and tear of property held by the taxpayer for the production of income, whether or not the property in question is used in the trade or business of the taxpayer, including a reasonable allowance for obsolescence. Except for this, the new allowance is subject to the same limitations and restrictions which have been applicable under this section prior to the present amendment.

The amendments made to the Code by this section are applicable to all taxable years beginning after December 31, 1938. These amendments shall also be effective as if they were a part of the Revenue Act of 1938 or any prior revenue act on the date of its enactment.

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.23 (a)-15 (as inserted by T. D. 5196, 1942-2 Cum. Bull. 96, 97-100, and amended by T. D. 5280, 1943, Cum. Bull. 1022, and T. D. 5331, 1944-4, Int. Rev. Bull. 4). *Nontrade or Nonbusiness Expenses.—(a) In general.* Subject to the qualifications and limitations in Chapter 1 and particularly in section 24, as amended, an expense may be deducted under section 23 (a) (2) only upon the condition that:

(1) it has been paid or incurred by the taxpayer during the taxable year (i) for the production or collection of income which, if and when realized, will be required to be included in income for Federal income tax purposes, or (ii) for the management, conservation, or maintenance of property held for the production of such income; and

(2) it is an ordinary and necessary expense for either or both of the purposes stated in (1) above.

The term "income" for the purpose of section 23 (a) (2) comprehends not merely income of the taxable year but also income which the taxpayer has realized in a prior taxable year or may realize in subsequent taxable years; and is not confined to recurring income but applies as well to gains from the disposition of property. For example, if defaulted bonds, the interest from which if received would be includible in income, are purchased with the expectation of realizing capital gain on their resale, even though no current yield thereon is anticipated, ordinary and necessary expenses thereafter incurred in connection therewith are deductible. Similarly, ordinary and necessary expenses incurred in the management, conservation or maintenance of a building devoted to rental purposes are deductible notwithstanding that there is actually no income therefrom in the taxable year, and regardless of the manner in which or the purpose for which the property in question was acquired. Expenses incurred in managing, conserving, or maintaining property held for investment may be deductible under this provision even though the property is not currently productive and there is no likelihood that the property will be sold at a profit or will otherwise be productive of income and even though the property is held merely to minimize a loss with respect thereto. The expenses, however, of carrying on transactions, which do not constitute a trade or business of the taxpayer and are not carried on for the production or collection of in-

come or for the management, conservation, or maintenance of property held for the production of income, but which are carried on primarily as a sport, hobby, or recreation are not allowable as nontrade or nonbusiness expenses.

Expenses, to be deductible under section 23 (a) (2), must be "ordinary and necessary," which presupposes that they must be reasonable in amount and must bear a reasonable and proximate relation to the production or collection of taxable income or to the management, conservation, or maintenance of property held for the production of income.

(b) Except for the requirement of being incurred in connection with a trade or business, a deduction under this section is subject to all the restrictions and limitations that apply in the case of the deduction under section 23 (a) (1) (A) of an expense paid or incurred in carrying on any trade or business. This includes restrictions and limitations contained in section 24, as amended. Section 24 (a) (5), as amended, continues to disallow any amount otherwise allowable as a deduction (whether under section 23 (a) (2) or otherwise) which is allocable to one or more classes of tax-exempt income, other than interest, and has the effect in addition of disallowing a deduction under section 23 (a) (2) for amounts otherwise allowable under that section which are allocable to tax-exempt interest.

Thus any amount allocable to the production or collection of one or more classes of income which is not includible in gross income or to the management, conservation or maintenance of property held for the production of such income is not deductible under section 23 (a) (2). Nor does section 23 (a) (2) allow any expenses which are disallowed by any of the provisions of Chapter 1 of the Code.

Capital expenditures, and expenses of carrying on transactions which do not constitute a trade or business of the taxpayer and are not carried on for the produc-

tion or collection of income or for the management, conservation, or maintenance of property held for the production of income, but which are carried on primarily as a sport, hobby, or recreation are not allowable as nontrade or nonbusiness expenses. The question whether or not a transaction is carried on primarily for the production of income or for the management, conservation, or maintenance of property held for the production or collection of income, rather than primarily as a sport, hobby, or recreation, is not to be determined solely from the intention of the taxpayer but rather from all the circumstances of the case, including the record of prior gain or loss of the taxpayer in the activity, the relation between the type of activity and the principal occupation of the taxpayer, and the uses to which the property or what it produces is put by the taxpayer.

Among expenditures not allowable under section 23 (a) (2) are the following: Commuters' expenses; expenses of taking special courses or training; expenses for improving personal appearance; the cost of rental of a safe-deposit box for storing jewelry and other personal effects; and expenses such as expenses in seeking employment or in placing oneself in a position to begin rendering personal services for compensation, campaign expenses of a candidate for public office, bar examination fees and other expenses incurred in securing admission to the bar, and corresponding fees and expenses incurred by physicians, dentists, accountants, and other taxpayers for securing the right to practice their respective professions.

Fees for services of investment counsel, custodian fees, clerical help, office rent, and similar expenses paid or incurred by a taxpayer in connection with investments held by him are deductible under section 23 (a) (2) only if (1) they are paid or incurred by the taxpayer for the production or collection of income, or for the management, conservation, or maintenance of investments held by him for the production of income;

and (2) they are ordinary and necessary under all the circumstances, having regard to the type of investment and to the relation of the taxpayer to such investment.

Ordinary and necessary expenses paid or incurred in connection with the management, conservation, or maintenance of property held for use as a residence by the taxpayer are not deductible. However, ordinary and necessary expenses paid or incurred in connection with the management, conservation, or maintenance of property held by the taxpayer as rental property are deductible even though such property was formerly held by the taxpayer for use as a home.

Expenditures incurred by an administrator or executor in securing the processes and orders of the court having jurisdiction over the probate of the estate, or in collecting the assets of the estate (other than income which, if and when realized, must be reported by the estate for income tax purposes), or in adjusting claims against the decedent, or in distributing the remaining assets to the beneficiaries, or in conserving the assets for ultimate distribution to the parties entitled thereto, are not deductible under this section. Ordinary and necessary expenses, however, which are paid or incurred during the taxable year by an administrator or executor for the production or collection of income which, if and when realized, must be reported by the estate for income-tax purposes, such as fees for collecting rents on property in the estate of the decedent, or for collecting interest or dividends on securities in that estate, or which are paid or incurred during the taxable year for the management, conservation, or maintenance of property in the estate of the decedent held for the production of income, the income from which, if and when realized, must be reported by the estate for income tax purposes, such as expenditures for insurance or repairs, or expenditures of a similar nature, are deductible under this section at the option of the taxpayer notwithstanding that deductions there-

for are allowable under section 812 (b) in computing the gross estate subject to the estate tax, provided the requisite statement and waiver are filed. (See section 162 (e).)

The ordinary expenditures of administration incurred in a receivership or bankruptcy proceeding are not deductible. Such expenditures include expenditures incurred in the performance of the ordinary duties of a receiver or trustee in bankruptcy, as, for example, fees paid to the attorney for the petitioning creditors, fees paid to the appraisers, and disbursements which are made in connection with the proceeding and which look toward the collection of the assets and their preservation pending ultimate distribution to the parties entitled thereto.

Reasonable amounts paid or incurred by a trustee on account of trustees' fees and other expenses which are ordinary and necessary in connection with the production or collection of trust income or with the management, conservation, or maintenance of trust property held for the production of income are deductible, notwithstanding that the trust is not engaged in a trade or business.

Reasonable amounts paid or incurred for the services of a guardian or committee for a ward or minor, and other expenses of guardians and committees which are ordinary and necessary, in connection with the production or collection of income inuring to the ward or minor, or in connection with the management, conservation, or maintenance of property, held for the production of income, belonging to the ward or minor, are deductible.

It is immaterial whether the expenses of fiduciaries are paid from the corpus of the estate or from income. Expenses derive their character not from the fund from which they are paid, but from the purposes for which they are incurred.

Expenditures incurred in defending or perfecting title to property, in recovering property (other than investment property and amounts of income which, if and when recovered, must be included in income), or in developing or improving property, constitute a part of the cost of the property and are not deductible expenses. Attorneys' fees paid in a suit to quiet title to lands are not deductible; but if the suit is also to collect accrued rents thereon, that portion of such fees is deductible which is properly allocable to the services rendered in collecting such rents. Expenditures incurred in protecting or asserting one's rights to property of a decedent as heir or legatee, or as beneficiary under a testamentary trust, are not deductible expenses. Expenditures incurred for the purpose of preparing tax returns (except to the extent such returns relate to taxes on property held for the production of income), for the purpose of recovering taxes (other than recoveries required to be included in income), or for the purpose of resisting a proposed additional assessment of taxes (other than taxes on property held for the production of income) are not deductible expenses under this section, except that part thereof which the taxpayer clearly shows to be properly allocable to the recovery of interest required to be included in income.

The deduction of an item otherwise allowable under section 23 (a) (2) will not be disallowed simply because the taxpayer also had an election under chapter 1 to treat it as a capital expenditure, rather than to deduct it as an expense. (See section 24 (a) (7), added by section 130 (a) of the Revenue Act of 1942.) Where, however, the item may properly be treated only as a capital expenditure or where it was properly so treated under an option granted in chapter 1, no deduction is allowable under this section; and this is true regardless of whether any basis adjustment is allowed under section 113.

(c) The provisions of section 23 (a) (2) are not intended in any way to disallow expenses which would otherwise be allowable under section 23 (a) (1) or the regulations applicable thereto, or under any other section of the Internal Revenue Code or the regulations applicable thereto. Double deductions are not permitted. Amounts deducted under one provision of the Internal Revenue Code can not again be deducted under any other provision thereof.

SEC. 19.24-2 (as amended by T. D. 5166, 1942-2 Cum. Bull. 87). *Capital expenditures.*—Amounts paid for increasing the capital value or for making good the depreciation (for which a deduction has been made) of property are not deductible from gross income. (See section 23 (l).) Amounts expended for securing a copyright and plates, which remain the property of the person making the payments, are investments of capital. The cost of defending or perfecting title to property constitutes a part of the cost of the property and is not a deductible expense. The amount expended for architects' services is part of the cost of the building. Commissions paid in purchasing securities are a part of the cost price of such securities. Commissions paid in selling securities are an offset against the selling price, except that in the case of dealers in securities such commissions may be treated as an ordinary and necessary business expense. Expenses of the administration of an estate, such as court costs, attorneys' fees, and executors' commissions, are chargeable against the corpus of the estate and are not allowable deductions. Amounts to be assessed and paid under an agreement between bondholders or shareholders of a corporation, to be used in a reorganization of the corporation, are investments of capital and not deductible for any purpose in returns of income. (See section 19.22 (a)-17.) An assessment paid by a shareholder of a national bank on account of his statutory liability is ordinarily not deductible but, subject to the provi-

sions of the Internal Revenue Code, may in certain cases represent a loss. Expenses of the organization of a corporation, such as incorporation fees, attorneys' and accountants' charges, are capital expenditures and not deductible from gross income. A holding company which guarantees dividends at a specified rate on the stock of a subsidiary corporation for the purpose of securing new capital for the subsidiary and increasing the value of its stock holdings in the subsidiary may not deduct amounts paid in carrying out this guaranty in computing its net income, but such payments may be added to the cost of its stock in the subsidiary.